AML, CTF & Sanctions Guidance Part II

Subject: Private Banking

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Preface

This part of the AML, CFT & Sanctions Guidance comprises Private Banking specific additional guidance focused on ML/TF risks and complements the general Guidance in Part I. Specific sanctions risks related to Private Banking are not (yet) addressed in this part of the guidance and will be further developed. Please refer to Part I chapter 4 for the general section on Sanctions.

This part is incomplete on its own and must be read in conjunction with the main guidance set out in Part I of this AML, CFT & Sanctions Guidance. Please refer to the Preface of Part I for the applicable regulatory framework and the purpose and the scope of the Guidance.

4. Private Banking

Introduction

General Overview and Due Diligence

4.1. Private Banking is the provision of banking and other investment services including advice, discretionary fund management and brokerage to private investors, ranging from the mass affluent to high and ultra-high net worth individuals (HNWI and UHNWI) and their families or businesses to sustain and grow long-term wealth. It is also known as Wealth Management (see EBA, ESMA Joint Guidelines 2017, chapter 5 point 143).

4.2 Although Private Banking is identified as inherently high risk, it does not necessarily mean that all customers serviced by Private Banking have to be considered higher risk.Private Banking customers must be subject to EDD measures, which may entail the application of the following requirements (not limited to):

- Verifying the source of funds and/or wealth; see Part I Chapter 2.3.
- Establishing the destination of funds;
- Ensuring that a customer's use of complex business structures such as trusts and private investment vehicles is for legitimate and genuine purposes.

AML/CTF Risks

General

4.3 Private Banking entails potentially higher integrity risks. In general these customers are very wealthy and often use more complex products and complex (tax-driven) structures. This follows, Annex III 4AMLD and art. 8 of the Wwft that states that EDD should be undertaken with reference to the Annex.

Inherent Risks in Private Banking

4.4 Money launderers are attracted by the availability of specialised products and the provision of services that operate internationally, utilise detailed knowledge of customers create a

secure and reputable private banking environment and are familiar with transactions for private investors. This generates a layer of respectability that 'covers' criminal activity and, it is felt, protects it from investigation. The following factors contribute to the vulnerability of private banking:

- Wealthy and powerful customers: Such customers may be reluctant or unwilling to provide adequate documents, details and explanations. The situation with regard to them is exacerbated where the customer enjoys a high public profile, and may fall into the category of Politically Exposed Person (PEP), indicating that they wield or have recently wielded political or economic power or influence.
- Multiple and complex accounts: wealthy customers often have many accounts in more than one jurisdiction, either within the same bank or group, or with different financial institutions. In the latter situation it may be more difficult for relationship managers to accurately assess the true purpose and business rationale for individual transactions.
- Cultures of confidentiality: better off private banking customers may seek extra reassurance that their need for confidential business will be conducted discreetly will be met. However, requests for confidentiality should not lead to unwarranted levels of secrecy that suit those with criminal intentions or interfere with regulatory requirements.
- Concealment: The use of services such as offshore trusts and the availability of structures such as shell companies in some jurisdictions helps to maintain an element of secrecy about beneficial ownership of funds and may give rise to significant misuse. Care should be taken to ensure that use of banking and investment services in such countries does not facilitate the development of layers of obscurity that assist those with criminal intentions.
- Jurisdictions maintaining statutory banking secrecy: there is a culture of secrecy in some jurisdictions, supported by local legislation, in which private banking customers may hold accounts without being detected as doing so; it is very difficult if not impossible to investigate whether these accounts have been used for laundered money.
- Corrupt jurisdictions: there are jurisdictions where corruption is known, or perceived, to be a common method of acquiring personal wealth. Attempts may be made to launder assets gained from corrupt practices in these jurisdictions through wealth management services.

- Movement of funds: The transmission of funds and other assets by private customers may involve high value transactions, and rapid transfers of wealth across accounts in different countries and regions of the world; this can facilitate the concealment of illicit funds before the authorities can catch up with them.
- The use of concentration accounts: i.e. multi-customer pooled/omnibus type accounts these are used to collect together funds from a variety of sources for onward transmission and can hide laundered money in the pooling; they are seen as a potential major risk.
- Credit: the extension of credit to customers who use their assets as collateral also poses a money laundering risk unless the lender is satisfied that the origin and source of the underlying asset is legitimate.

4.5 Secured loans where collateral is held in one jurisdiction and the loan is made from another are common in the private banking areas. Such arrangements may serve a legitimate business function and make possible certain transactions which may otherwise be unacceptable due to credit risk. But they may also make it easier to conceal the sources of illicit funds. Collateralised loans raise different legal issues depending on the jurisdiction of the loan, but foremost among these issues are the propriety and implications of guarantees from third parties (whose identity may not always be revealed) and other undisclosed security arrangements that may hide the true nature of the collateral. Particular care should be taken where the lender is relying upon the guarantee of a third party not otherwise in a direct customer relationship, and where the collateral is not in the same jurisdiction as the lending firm.

Assessment of the Risk

4.6 The role of the relationship manager is particularly important to the private bank in managing and controlling and mitigating the money laundering or terrorist financing risks it faces. Relationship managers develop strong personal relationships with their customers, which facilitates the collection of the necessary information to know the customer's business and financial affairs, including knowledge of the source(s) of the customer's wealth. However, wealthy customers can have business affairs and lifestyle that may make it difficult to establish what is "normal" and therefore what may constitute unusual behaviour.

4.7 Relationship managers must, however, at all times be alert to the risk of becoming too close to the customer and to guard against the risks from:

- A false sense of security;
- Conflicts of interest which may compromise the firm's ability to meet its AML obligations and its wider financial crime responsibilities;
- Undue influence by others, especially by the customers themselves.